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Supreme Court of the United States

October Term, 1945

No. 384

FORREST S. SMITH, Trustee of the Property of Hoboken Manufacturers Railroad Company, Debtor, *et al.*,
Petitioners,

vs.

HOBOKEN RAILROAD WAREHOUSE AND STEAMSHIP CONNECTING COMPANY and HOBOKEN LAND AND IMPROVEMENT COMPANY,
Respondents.

BRIEF FOR RESPONDENTS IN OPPOSITION TO APPLICATION FOR WRIT OF CERTIORARI

EDWARD J. O'MARA,
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Opinions of the Courts Below.

The opinion of the Circuit Court of Appeals for the Third Circuit is not yet reported, but is printed page 116 of the record. The opinion of the District Court was reported in 56 Fed. Sup. 187 and is printed page 55 of the record.

Statement of the Case.

Petitioners' statement of the case is such that it requires amplification.

On June 19, 1906, Hoboken Railroad, Warehouse and Steamship Connecting Company (hereinafter called Connecting Company) leased to the debtor a line of railroad, including all rights of way, roadbed, tracks, rails, ties,

freight-houses, terminals, yards, engine-houses, car and machine shops, rolling stock and other equipment, in the City of Hoboken, New Jersey, for a period of ninety-nine years. Article Third, paragraph (1), of the lease provides:

> "The Lessee shall not and will not sell, assign or transfer this lease or underlet the demised premises, or any part thereof, or the rights and privileges, or any of them, hereby granted, without the previous consent of the Lessor expressed by endorsement on this lease made in pursuance of authority granted by resolution of the board of directors of the Lessor, * * *. This covenant shall also apply to any unauthorized sale or transfer thereof or underletting of the demised premises, or any part thereof, or of the said rights and privileges, or any of them, whether made by the Lessee or in any proceeding, whether at law or in equity or otherwise, to which the Lessee may be a party, whereby any of the rights, duties and obligations of the Lessee shall or may be transferred, encumbered, abrogated or in any manner altered, without the consent of the Lessor first had and obtained in the manner hereinbefore provided" (R. 84a).

The Fifth Article of the lease provided that upon the failure to observe, keep and perform the covenants and agreements thereof, after such default had continued for a space of thirty days after notice from the lessor thereof, the lessor might at its option by notice in writing terminate the lease and thereupon enter into and upon the demised premises and that the right, title and interest of the lessee should thereupon absolutely cease and terminate as though the lease had never been made (R. 93).

The rental reserved by the lease was the sum of several items as follows:

(1) A stated amount of $22,000.00 per year (later reduced to $21,500.00 per year)

(2) An amount per ton of freight transported over a certain amount, as specified in the lease, and referred to as "excess tonnage"

(3) All premiums of insurance upon the leased premises.

(4) All taxes upon the demised premises or upon the lessor by reason of its ownership thereof, and of the appurtenant franchises, or upon the rent reserved by the lease and which the lessee may be required to pay thereon or retain or deduct therefrom under any present or future law.

Up to the time of filing the petition for reorganization herein, the debtor had paid the lessor the base rental of $21,500.00 fixed by the lease and had reimbursed it for insurance premiums. It refused to pay Federal income and excess profits taxes levied against the lessor, and certain excess tonnage, claiming that such taxes and tonnage did not come within the terms of the lease (R. 17a). The lessor thereupon demanded arbitration under a clause of the lease providing therefor, and the arbitrators made an award against the debtor in the total amount claimed by the lessor, namely $24,102.43 (for the fiscal years beginning July 1, 1932 and ending June 30, 1939). The lessor thereupon commenced an action at law in the Hudson County Court of Common Pleas to recover the amount of the arbitrators' award, and the debtor filed a bill in the New Jersey Court of Chancery to restrain the prosecution of the action. The Chancery suit was determined adversely to the debtor, which thereupon appealed to the Court of Errors and Appeals. That court affirmed the Court of Chancery and on or about July 2, 1943, lessor entered judgment in its action at law in the Hudson County Court of Common Pleas against the debtor in the amount of $27,965.00. In the meantime,

and on or about March 31, 1943, the lessor instituted a second action at law in the Hudson County Court of Common Pleas for additional rental for the fiscal years ending June 30, 1940, 1941 and 1942 in the amount of $14,566.44 (R. 18a).

On July 26, 1943, a little more than three weeks after the entry of the aforesaid judgment, the debtor filed its petition for reorganization in the United States District Court for the District of New Jersey, alleging among other things that the financial condition of the debtor was seriously aggravated by the entry of the lessor's judgment for rent and the pending suit for additional rent (R. 16a, 17a, 18a). The petition also alleged that the debtor had no means of borrowing or otherwise procuring funds to meet its obligations, and that its cash reserves were wholly insufficient for its financial requirements including necessary working capital, and that therefore the debtor was without funds to continue to operate the railroad and property and maintain the same in condition and repair to render adequate service to the public and at the same time meet its debts (R. 21a). The court made an order approving the petition on the day it was filed. Thereafter, Forrest S. Smith was appointed trustee and after the approval of his appointment by the Interstate Commerce Commission, he duly qualified and entered upon the performance of his duties as such trustee on November 12, 1943. On February 14, 1944, the lessor moved for an order modifying the restraints imposed by Order No. 1 (approving the petition for reorganization) so as to permit the lessor to terminate the lease for breach of covenant (R. 40a). After oral argument on the motion, the court ordered briefs, and on August 4, 1944, handed down its opinion authorizing such termination (R. 55a). In the interim and on June 12, 1944, the court entered Order No. 27 (R. 51a) on the petition of the trustee (R. 48a), authorizing the trustee to adopt the

lease and other executory contracts, and pursuant thereto the trustee served notice upon the lessor that he had elected to adopt said lease (R. 52a).

The district court's opinion on the motion to terminate the lease granted the relief sought, to take effect upon production to the court of conclusive evidence that the requirements of the laws relating to the continuous operation of the railroad had been complied with (R. 59a). The lessor thereupon filed a petition with the Interstate Commerce Commission, setting forth the circumstances of the case, and praying for a determination by the Commission that the lessor did not require a certificate of convenience and necessity to resume operation of the railroad. The trustee, the debtor, and Seatrain Lines Inc. (the owner of all of the capital stock of the debtor) sought and obtained permission to intervene in said proceedings and filed briefs opposing the contention of the lessor. On December 2, 1944, the Interstate Commerce Commission filed its report, in which it found that the lessor did not require a certificate of convenience and necessity, and that it had not only the right but the duty to resume the operation of the railroad without such certificate (R. 66a et seq.). Thereafter, and on December 19, 1944, Order No. 39 (R. 76a) was entered in the District Court, authorizing the lessor to terminate the lease and enter into possession as of midnight, December 31, 1944, and on July 17, 1945, the said order was affirmed by the Circuit Court of Appeals for the Third Circuit.

Summary of Argument.

Respondents respectfully submit that the petition for a writ of certiorari should be denied because:

1. The qualification of the trustee and his subsequent adoption of the lease breached the covenant against assignment and entitled the landlord to terminate the lease.

2. There is not here involved an important question of Federal Law which has not been but should be decided by this Court.

3. Order No. 39 should not be reversed because it transfers possession of certain railroad property, claimed by the trustee, to the lessor before determination of title thereto.

4. The District Court did not err in failing to require the landlord to obtain a certificate of convenience and necessity under Section I (18) of the Interstate Commerce Act or in requiring the trustee to discontinue operations without prior approval by the Interstate Commerce Commission authorizing such discontinuance.

ARGUMENT.

POINT I.

The qualification of the trustee and his subsequent adoption of the lease breached the covenant against assignment and entitled the landlord to terminate the lease.

Article Third, paragraph (1), of the lease provides:

> "The Lessee shall not and will not sell, assign or transfer this lease or underlet the demised premises, or any part thereof, or the rights and privileges, or any of them, hereby granted, without the previous consent of the Lessor expressed by endorsement on this lease made in pursuance of authority granted by resolution of the board of directors of the Lessor, * * *. This covenant shall also apply to any unauthorized sale or transfer thereof or underletting of the demised premises, or any part thereof, or of the said rights and privileges, or any of them, whether made by the Lessee or in

any proceeding, whether at law or in equity or otherwise, to which the Lessee may be a party, whereby any of the rights, duties and obligations of the Lessee shall or may be transferred, encumbered, abrogated or in any manner altered, without the consent of the Lessor first had and obtained in the manner hereinbefore provided" (R. 84a).

It will be seen that the lessor, by the broadest possible language, sought by this covenant to prevent any transfer of the lessee's rights or obligations under the lease without the consent of the lessor expressed by endorsement on the lease pursuant to a resolution of its board of directors. The covenant prohibited not only a voluntary transfer of the lessee's interests, but also any transfer made in any proceeding, whether at law or in equity or otherwise, to which the lessee was a party, whereby any of the rights, duties and obligations of the lessee should or might be transferred, encumbered, abrogated or in any manner altered. This contract was voluntarily assumed by both parties. The lease is a carefully drawn instrument covering thirty-two printed pages exclusive of the schedules. At the time of its execution, the lessor had acquired railroad operating rights, a charter from the State of New Jersey, and a franchise from the City of Hoboken enabling it to operate the railroad. It had constructed the railroad and had operated it for nine years, thereby establishing a going business. By this instrument it leased a fully equipped and going railroad to a lessee of its choice in the full knowledge that it as the owner was obligated to resume and perform the operation of the road at any time that its lessee defaulted or became unable to operate. Recognizing the possibility of the sudden reversion of the railroad to it at any time, the lessor in Article Third (b) of the lease (R. 82a) required the lessee to efficiently maintain and operate the

railroad and to enlarge and improve it in consonance with the growth of the district which it served and the increased traffic available to it. The lessee was required under the lease to keep the railway system of the lessor equipped with a sufficient number of engines, electric motors and cars, and with all the electrical and other power appliances that might be needed, "so that in case of the termination of this indenture at any time, the demised premises shall be adequately furnished and equipped to carry on business and continue its operations" (R. 83a).

The lessor, like any other landlord, had a property owner's right to select the tenant who would occupy and use, and who would be charged with the obligation of preserving, protecting and improving the leased property. It likewise had the right to insist that no other party should succeed to the lessee's rights and obligations without its consent. This right was far more important to it than it would be to the lessor of an ordinary piece of real estate. It was leasing a going railroad—a costly one-use property which might easily become a money losing proposition, with the consequent degeneration of its plant and equipment, if it were not well managed and if its freight traffic were not stimulated and elevated to a high level. It was charged with the public duty of operating the road in the event of the default or inability of the lessee to continue operation. It was of the utmost importance, therefore, that it should contract only with a lessee of its choice, and that the obligations assumed by the lessee should not be transferred to a third party without the lessor's consent. The lessor guarded against such transfer by the sweeping language employed in the covenant hereinabove set forth, and the lessee freely and willingly executed the lease with that covenant contained therein.

Appellants argue that an ordinary covenant against assignment is not breached by the bankruptcy of the lessee

and the consequent transfer of his interest to a trustee. We are in accord with that proposition. In *re Prudential Lithograph Company*, 265 Fed. 869; (D. C. S. D. N. Y.) in *re Levinson*, 295 Fed. 140 (D. C. W. D. Wash. N. D.). It is equally well established, however, that a clause specifically giving the lessor the right to terminate the lease upon the filing of a petition in bankruptcy by or against the lessee is enforceable. In *re Wil-low Cafeterias*, 95 F. (2d) 306 (C. C. A. 2nd Circuit).

In *Model Dairy Co.* v. *Foltis-Fischer Inc.* (C. C. A., 2nd Cir.) 67 F. (2d) 704, the court upheld a clause in the lease permitting the lessor to reenter on the tenant's insolvency, bankruptcy or receivership, saying at page 706:

> "It is true that courts do not look upon such conditions with a friendly eye, classing them as forfeitures. * * * Nevertheless they are valid, and we must give effect to the fair meaning of the language used. * * * The receiver, though not truly a tenant, is in possession and prevents him" (the lessor) "from disposing of the premises as he would. Unless the lease contains a condition against passage of title, he must suffer the term to be sold to one whom he may not desire."

In *Jandrew* v. *Bouche*, 29 F. (2d) 346 (C. C. A., 5th Cir.), the lease contained a stipulation against its assignment without the consent of the lessor, and, among other things, that the lessee "shall not permit or suffer any of the goods, * * * or other personal property which may be on the said premises at any time during the period of said lease to be seized under any legal process or to pass into the hands of any receiver or trustee in bankruptcy or other officer, and that this lease shall be personal to the lessees and shall not inure to the benefit of any receiver or trustee in bankruptcy as an asset of the said lessees." The court held that the last quoted clause was one of conditional limi-

tation, *ipso facto* terminating the lease, without action by either party, with the adjudication in bankruptcy and the appointment of the trustee.

In *In re Georgalas Bros.*, 245 Fed. 129 (D. C., N. D. Ohio), the trustee in bankruptcy claimed the right to sell a lease which the lessor claimed was void. The lease contained a provision that "if the lessee shall be adjudged bankrupt; or shall make an assignment for the benefit of his creditors, or if this lease shall pass by transfer, operation of law, or otherwise from said lessee to any other party without the written consent of the lessor", the lessor may void the lease and reenter. The question before the court was whether the lease had passed "by operation of law or otherwise from said lessee to any other person without the written consent of the lessor." The court concluded that the lessor had the right to avoid the lease, saying, page 131:

> "It is not asserted that the lessor had consented, in writing or otherwise, to the transfer of this lease by operation of law to the trustee. The only right of the trustee to sell the lease is by virtue of the transfer thereof by operation of law to him. It is inconsistent to assert title in the trustee by operation of law, and yet to say that the title still remains in Theodore, and that the covenant is not broken. An adjudication in bankruptcy against a partnership, it is settled law in this circuit, operates to transfer by law to the trustee all the property and assets of the individual members of the partnership. * * * It is by virtue of this legal effect of an adjudication of the partnership to be bankrupt that the trustee acquires a right or title to this lease. It is equally effective to operate as a transfer by operation of law of the lease, so as to bring about a violation of this covenant.
>
> "It is also settled law that a lease may be so framed that a transfer by operation of law will avoid the same at the option of the lessor. *Gazlay* v. *Williams*, 210 U. S. 41; *In re Frazin*, 183 Fed. 28. The covenant

above quoted, when properly interpreted and understood, bring the facts within its terms, and the lessor's right to avoid the same is well established, and is sustained by the authorities above cited."

In *Empress Theatre Co.* v. *Horton*, 266 Fed. 657 (C. C. A., 8th Cir.), the court upheld a clause in a lease that "no right, title or interest upon this lease shall pass to any trustee in bankruptcy, or by judicial process, or by operation of law, without the consent" of the lessor, and that "the bankruptcy or insolvency" of the lessee shall at the option of the lessor work an immediate forfeiture of the lease. The court said, page 661:

> "* * * The basement leased was a valuable property. The purpose the lessor had in making the lease, to secure the operation in this basement of a high class cafe with special amusement features, made the solvency of the lessee and hence its continuous operation of the cafe essential to the accomplishment of this purpose. Its insolvency or bankruptcy, placing the basement in the hands of a trustee for a long time during bankruptcy proceedings, and then sending it to an unknown purchaser, would undoubtedly to a large extent defeat the object of the lessor in making the lease, produce the vacancy or inadequate operation of the proposed cafe, and result in immeasurable damage to the leased premises and to the value of their use. It was to prevent this contemplated possibility that these parties wrote into their lease the condition and covenant that in case of the insolvency or bankruptcy of the lessee, at the election of the lessor, the term of the lease should end and the leased premises should be returned to the lessor free from the lease."

Petitioners contend, however, that the covenant herein is not a covenant against bankruptcy, nor a covenant providing for termination if the lessee should file a petition

in reorganization and that since the covenant should be construed strictly against the lessor, there has been no breach which would entitle the lessor to terminate the lease.

In *Gazlay* v. *Williams*, 210 U. S. 41, the Supreme Court held that a general clause against assignment prohibits only a voluntary assignment on the part of the lessee, and is not violated by a transfer by operation of law. The court recognized, however, that a covenant against assignment by operation of law was valid and enforceable, and quoted with approval Jones on Landlord and Tenant, as follows (p. 47):

> "* * * Jones, in his work on Landlord and Tenant, lays it down (Section 466) that 'An ordinary covenant against subletting and assignment is not broken by a transfer of the leased premises by operation of law, but the covenant may be so drawn as to expressly prohibit such a transfer, and in that case the lease would be forfeited by an assignment by operation of law'."

The same distinction is recognized by the Chandler Act (Act of June 22, 1938, c. 575 Section 1, 52 Stat. 879; U. S. C. A. Title 11, Section 110, paragraph b), which provides:

> "* * * A general covenant or condition in a lease that it shall not be assigned shall not be construed to prevent the trustee from assuming the same at his election and subsequently assigning the same; but an express covenant that an assignment by operation of law or the bankruptcy of a specified party thereto or of either party shall terminate the lease or give the other party an election to terminate the same, shall be enforceable * * *."

It may be conceded that the covenant here before the court is not literally a covenant against bankruptcy. It is, however, far broader than such a covenant. It gives

to the lessor the option to terminate the lease upon a sale or transfer, either by the voluntary act of the lessee or in any kind of legal proceeding to which the lessee is a party, whereby any of the rights, duties and obligations of the lessee shall or may be transferred, encumbered, abrogated or in any manner altered. The purpose of the clause cannot be open to doubt. It was the intention of the lessor to protect itself by the broadest possible language against the voluntary or involuntary transfer of the lessee's obligations under the lease to any other party, without the consent of the lessor. The word "unauthorized", as the context makes clear, relates to the lessor; and the clause operates to vest in the lessor an option to terminate the lease when the transfer of the lessee's interest is accomplished in any legal proceeding whatever, which was instituted without the previous consent of the lessor. The clause is in effect a prohibition against the transfer of the lessee's interest in the lease, either voluntarily or *by operation of law*. A transfer by operation of law is precisely what has happened in this proceeding.

By Order No. 5 herein appointing Forrest S. Smith trustee it was provided (Par. 6):

> "That following said ratification" (by the Interstate Commerce Commission) "and upon filing such bond, all of the property, real, personal and mixed of every kind and nature whatsoever of the debtor shall by this order be vested in the said Forrest S. Smith as trustee of the debtor's property." (R. 36a.)

This order was made pursuant to U. S. C. A. Title 11, Section 205, paragraph (c), subdivision (2), which provides:

> "* * * The trustee or trustees so appointed, upon filing such bond, shall have all the title and shall exercise, subject to the control of the judge and con-

sistently with the provisions of this section, all of the powers of a trustee appointed pursuant to Section 72 or any other section of this title, and, to the extent not inconsistent with this section, if authorized by the judge, the powers of a receiver in an equity proceeding, and, subject to the control of the judge and the jurisdiction of the Commission as provided by Chapter 1 of Title 49 as on August 27, 1935, or thereafter amended, the power to operate the business of the debtor."

Paragraph (1) of the same section provides:

"In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed."

Section 72 referred to in the above quotation is the section providing for the election of a trustee under the Bankruptcy Act. Consequently, by the very words of the statute the title which the trustee herein acquired by virtue of his trusteeship, is exactly the kind of title which a trustee in an ordinary bankruptcy acquires.

It is well settled that upon adjudication in bankruptcy, all the property of the bankrupt vests in the trustee as of the date of the filing of the petition. *Isaacs, Trustee* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734; *Gross* v. *Irving Trust Company*, 289 U. S. 342; *Irving Trust Company* v. *Perry*, 293 U. S. 307; *Taylor* v. *Sternberg*, 293 U. S. 470; *Armour & Company* v. *Callahan*, 25 F. (2d) 584 (C. C. A. 4th Cir.); *In re Levinson*, 295 Fed. 146 (D. C. Wash.).

It seems clear, therefore, that under the statute the title to the lessee's interest in the lease became vested in the trustee, if not upon his qulaification, certainly upon his adoption of the lease. *Palmer* v. *Palmer*, 104 F. (2d) 161 (C. C. A. 2nd Cir.). We therefore have an unauthorized transfer of the demised premises and of the rights and privileges of the lessee made in a proceeding "whether at law or in equity or otherwise" to which the lessee was a party, and by virtue of which the rights, duties and obligations of the lessee were transferred, abrogated and altered.

It is evident that the rights, duties and obligations of the lessee were transferred, abrogated and altered by the vesting of the title in the trustee. The lessee's obligation to pay the rental was transferred to the trustee. The duty imposed upon the lessee of operating the railroad was transferred to the trustee. Its obligation to maintain and improve the railroad and to keep it properly equipped, so that it could handle the expanded traffic in harmony with the growth of the community it served, passed from the lessee to the trustee. The duty imposed upon the lessee to stimulate the traffic of the railroad and to protect the lessor's operating rights likewise passed to the trustee. In fact, all of the rights the lessee acquired and all of the duties and obligations it assumed by virtue of the lease, passed from the lessee to the trustee, without the consent of the lessor. Thus the very situation which the lessor was careful to guard against by the inclusion of the covenant in the lease, was consummated.

In *Finn, Trustee* v. *Meighan*, 65 S. Ct. 1147, this court decided that a covenant in a lease terminating the tenancy if a petition in bankruptcy should be filed by the tenant, or if the tenant should be adjudged bankrupt or insolvent by any court, or if a trustee in bankruptcy of the tenant should be appointed in any suit or proceeding brought by or against the tenant, was breached upon the tenant's voluntary petition for reorganization under Chap-

ter X of the Bankruptcy Act and the approval of such petition by the court. This decision destroys the petitioners' argument that the purpose for which a trustee in reorganization acquires title to the debtor's assets differs from the purpose for which the trustee in an ordinary bankruptcy acquires title to the assets of the bankrupt, and that therefore the acquisition of title by a trustee in reorganization should not be considered a breach of a covenant against bankruptcy or, as in the case at bar, against the assignment of the tenant's interests in the leasehold in any proceeding at law, in equity or otherwise. Even if the law recognized the distinction for which petitioners contend, however, it would be utterly immaterial to this issue.

We are here concerned solely with the question of whether or not there was an unauthorized transfer of the lessee's rights, duties and obligations under the lease. The purpose of such transfer, the length of its duration, the possibility of a subsequent re-acquisition of the rights, duties and obligations by the lessee are entirely extraneous. The lessor used every precaution which care, prudence and ingenuity could suggest to prevent the transfer of the lessee's interest to any third party for any purpose whatever. The moment such a transfer took place, the lessor's substantial right to choose the one party to which it was willing to entrust the operation, maintenance and development of its property, which right the parties to this lease by their voluntary act agreed to protect, was violated. It is no answer to say that the violation might be cured in the indefinite future. It might or it might not be.

The duties and obligations of the lessee have been abrogated since July 26, 1943. The trustee has been operating the railroad since his qualification. One of the most important provisions of this lease is that in Article Third, by the terms of which the lessee is required not only to maintain the railroad, but to improve it so as to enable it to take

advantage of the increased business which the growth of the community would provide. Obviously, the lessor was entitled to the observance of this covenant by the lessee. It was undoubtedly one of the primary reasons why it was so careful to limit its contractual relationship to the lessee or to any substitute for the lessee which it should approve. It is equally obvious that the trustee could not, even if he desired to, perform the obligations of this covenant during the trusteeship. He could not be concerned with the long-range prospects of the railroad, as could a lessee under a lease which still had sixty years to run. His duty and his obligation is to preserve the assets as they exist, in the hope that a reorganization can be accomplished. That means that for all practical purposes he is operating on a day to day and hand-to-mouth basis. It is evident, therefore, that during the trusteeship the lessor has been and will be deprived of the perforamnce of the lessee's covenant to not merely operate the road but to improve the plant and expand its traffic.

To summarize, there has been a transfer of the lessee's interest in the lease in a legal proceeding to which it was a party, by virtue of which the rights, duties and obligations of the lessee passed to the trustee. The District Judge held that that transfer took place upon the qualification of the trustee (R. 59a). Even if this court should disagree with the court below on that point, it cannot be gainsaid that such a transfer certainly took place upon the trustee's adoption of the lease (*Palmer* v. *Palmer, supra*). The transfer took place without the consent of the lessor. We submit, therefore, that the covenant contained in Article Third (1) has been breached, and that the lessor is entitled to terminate the lease in accordance with the terms thereof.

POINT II.

There is not here involved an important question of Federal Law which has not been but should be decided by this Court.

The sole question presented here is whether or not the particular covenant contained in this lease was violated by the qualification of the trustee and his adoption of the lease.

Petitioners contend that, even if the District Court was correct in holding that the Connecting Company had a legal right to terminate its lease, entry of the termination order before considering any reorganization plan was premature. This argument is based upon the distinction between the purpose of an ordinary bankruptcy and that of a railroad reorganization proceeding. Excerpts from cases such as *Ecker* v. *Western Pacific Railroad Corp.*, 318 U. S. 448, and *Van Schaick* v. *McCarthy*, 116 F. (2d) 987 (C. C. A. 10th), which deal with the general principle that Section 77 contemplates the adoption of a suitable plan of reorganization rather than a liquidation of assets, are cited, and heavy reliance is placed upon the case of *Continental Bank* v. *Chicago, Rock Island etc. Ruy.*, 294 U. S. 648, wherein this court sustained the issuance of an injunction restraining the holders of collateral notes of the debtor, secured by bonds issued by it and its subsidiaries, from selling any of the collateral pending the preparation and consummation of a plan of reorganization.

In the *Rock Island* case, the court held that it could not impair the enforcement of the noteholder's contract, but under the general equity powers of the court could by its injunctive power delay its enforcement, so as not to defeat the purpose of Section 77. The application for the injunction was addressed to the discretion of the court under

its general equity powers and this court held that an appellate court would not interfere with the exercise of the lower court's discretion in the absence of a showing that it had been improvidently exercised.

The distinction between the *Rock Island* case and the case at bar, however, is obvious. The Rock Island system comprised over 8,000 miles of line, running through many states of the Union. It operated many subsidiaries, had a complicated capital structure, and there was outstanding a great volume of securities held by many and widely separated creditors with varying rights. The court found that it would be practically impossible to prepare any plan of reorganization the important details of which could survive the changes in and the consequent fluctuation and disturbance of the financial structure brought about by recurring sales of collateral, and consequently issued the injunction prayed for. It was manifestly important in that case that a plan of reorganization be worked out, if possible, which would preserve the railroad system as a going concern.

In the case at bar, however, the preservation of the operation of the railroad is not endangered. The lease herein involved is for an entire switching railroad, involving approximately nine miles of main stem track. The debtor has no complicated financial structure. It has no outstanding bonds or secured indebtedness. All of its capital stock is owned by Seatrain Lines Inc. (R. 16a). The petition for reorganization was filed with only one end in view, namely the forcing of the Connecting Company to agree to a new lease on more favorable terms to the debtor. The filing of the petition followed closely upon the entry of judgment against the debtor for unpaid rent under the lease and the institution of a suit for additional rent thereunder. It is evident both from the petition itself (R. 17a) and from a petition of the trustee filed on January 20,

1944 (R. 94) that the principal, if not the only reason for the filing of the petition was the inability of the debtor to pay the rent under the lease. It is apparent, therefore, that the only plan of reorganization which could be submitted by the debtor would involve a new lease on different terms. To that the lessor will never agree, and the injunctive power of the court should not be exercised for the purpose of awaiting the futile gesture of a plan of reorganization which can never be consummated. In effect, the court below refused to exercise such power and under the holding in the *Rock Island* case its discretionary decision in this regard should not be disturbed. To grant to the lessor the right to terminate its lease will not interfere with the primary purpose of Section 77 in the slightest degree, since all or substantially all of the railroad reverts to the lessor, which will instantly resume operation.

POINT III.

Order No. 39 should not be reversed because it transfers possession of certain railroad property, claimed by the trustee, to the lessor before determination of title thereto.

Petitioners complain that Order No. 39 should be reversed because it provides that all property of the debtor in the possession or under the control of the trustee and presently held or used for railroad purposes shall be delivered to the lessor, notwithstanding conflicting claims thereto, and that claimants might thereafter file a claim with the Clerk of the Court for the recovery of such property or its value and reasonable compensation for its use, which claims will thereupon be determined by the Court, through reference to a Master or otherwise.

This provision in the order was inserted at the suggestion of counsel for the trustee. It was an eminently prac-

tical suggestion, because the property in dispute, as is evident from the petitioners' brief, consists of two inconsequential lengths of track one about two hundred sixty-five feet in length, leading to a dead-end siding, and another about twenty feet long leading not to a float-bridge, as petitioners allege, but to a storage yard on land leased by debtor from the Delaware, Lackawanna and Western Railroad, which is of very little consequence in the operation of the railroad. The exclusion of either or both would not impair the lessor's ability to operate the railroad in the slightest degree. Of course, they were worthless to the trustee standing by themselves. Consequently the trustee through his counsel suggested the provision in the order of which petitioners now complain. The effect of the provision is to permit the continued operation of these small tracts in conjunction with the railroad, while the question of whether or not they revert to the lessor upon the termination of the lease is being determined by a Master. If it should be determined that they do not revert, the trustee under the terms of the order will be entitled to proper compensation for their use. If it is determined that they do revert as the respondents claim, no harm has come of the order.

It is not disputed that practically all of the railroad property reverts to the lessor on termination of the lease. The amount in dispute is less than one-tenth of one per cent of the property involved, and has no vital bearing upon the operation of the railroad. Even if the court were to permit the trustee to complain of a provision which he suggested, and should find that the court below had no technical right to include such a provision in the order, no basis would be formed for the reversal of the order. At most the order should be reformed by rescinding the provision complained of.

POINT IV.

The District Court did not err in failing to require the landlord to obtain a certificate of convenience and necessity under Section 1 (18) of the Interstate Commerce Act or in requiring the trustee to discontinue operation without prior approval by the Interstate Commerce Commission authorizing such discontinuance.

The District Judge granted the motion to terminate the lease upon production to the court of conclusive evidence that the requirements of the laws relating to the continuous operation of the railroad had been complied with (R. 59a). In order to satisfy this requirement, the lessor filed an application with the Interstate Commerce Commission to resume the operation of the railroad and in effect asked the Commission to find that the provisions of Section 1 (18) of the Act, requiring a certificate of necessity and convenience before operation could be undertaken, did not apply, since the lessor was merely resuming operation of its own properties after temporary suspension during the existence of the lease. The petitioners herein sought and obtained leave to intervene in the proceedings before the Commission, and filed briefs. The Commission held that no certificate was required by the lessor, since its obligations and duties to the public have never ceased, but have merely been performed by the lessee during the term of the lease (R. 66a). The Commission therefore found that, independent of any certificate of necessity and convenience, the lessor had not only the right but the positive duty to resume the operation of the railroad, and in accordance with that finding, entered an appropriate order dismissing the respondent's application for a certificate (R. 75a).

Petitioners did not seek a review of the order of the Interstate Commerce Commission, but attempt to attack it

collaterally herein. It is respectfully submitted that they will not be heard to do so. The purpose of the District Judge was to assure the continuous operation of the Railroad. From the time of the institution of the proceedings to terminate the lease, the landlord has always recognized and now recognizes its obligation to take over such operation. Petitioners objected before the District Court that it would not be legally possible for the landlord to do so without securing from the Interstate Commerce Commission a Certificate of Convenience and Necessity. Out of a super-abundance of caution, the District Judge withheld the entry of the order terminating the lease for many months until the Interstate Commerce Commission should pass upon whether or not such a certificate was necessary. The decision of the Interstate Commerce Commission that it was not was reached after a full consideration of the matter, in which the petitioner sought and obtained the right to intervene and to file briefs.

It is not the petitioners' function to protect whatever public interest is involved in this matter. That is a matter solely between the Interstate Commerce Commission and the landlord. The landlord is ready, able and willing to resume the operation of the Railroad at a moment's notice. If the Interstate Commerce Commission was wrong in holding that no Certificate of Convenience and Necessity is necessary, it will have ample opportunity to correct the error.

CONCLUSION.

It is respectfully submitted that for the foregoing reasons the petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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